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E.O. 12958: DECL: 09/30/2019
TAGS: ECON EFIN VE
SUBJECT: ANOTHER BOND ISSUANCE TARGETS THE PARALLEL MARKET

REF: A. 2008 CARACAS 376
¶B. CARACAS 548
¶C. CARACAS 1228

Classified By: Economic Counselor Darnall Steuart for reasons 1.4 (b) and (d).

¶1. (U) The Venezuelan government (GBRV) announced on September 28 and 29 the terms for the planned issuance of USD 3 billion in dollar-denominated bonds (Bonos Soberanos Internacionales). Half the bonds will mature in 2019 and half in 2024, and all will be Eurobonds registered in Luxembourg. As in recent past issuances of dollar-denominated bonds, buyers will purchase them from the GBRV in bolivars (Bs). In effect, the government is supplying dollar instruments to the parallel foreign exchange market in an attempt to bring down the parallel rate, as it has done in numerous past issuances (ref A). Bids will be accepted at prices between 135 and 140 percent of par (at the official exchange rate), which translates into an implicit exchange rate of between 3.9 and 4.3 Bs/USD, depending on the estimated yield of the bonds in international markets. The GBRV will accept bids through October 2 and announce the results October 6. (Note: At the official exchange rate of 2.15 Bs/USD, a bid of 140 percent of par translates into a price of Bs 3 per USD of par value purchased (1 USD x 2.15 Bs/USD x 140 percent = Bs 3). Assuming a yield of roughly 12.5 percent (the current yield of similar GBRV bonds, which would give an average price of USD 76 for each USD 100 of par value) and a commission of 1 percent, one analyst calculated an implicit exchange rate to be 4 Bs/USD. A yield of 13.5 percent would, this analyst estimates, give an implicit exchange rate of 4.3 Bs/USD. The parallel rate on October 1 was 5.5 Bs/USD. End note)

¶2. (C) Bernardo Chacin (strictly protect throughout), president of Citibank Venezuela, told EconCouns on September 28 that Venezuelan Central Bank (BCV) president Nelson Merentes was the driving force behind issuance. (Note: Citigroup is one of the two banks coordinating the issuance, and Chacin had frequent contact with GBRV and BCV officials in the run-up to the announcements. End note.) He said Merentes had caused the bond to be priced "to send a strong signal" to players in the parallel market. Chacin noted he expected the GBRV would raise the amount of the issuance to USD 4 billion, and there are rumors it could be even higher. Finally, Chacin commented that the GBRV's acting Director of Public Credit had insisted the issuance be concluded by early October because, in her words, "the government needs money." (Note: At a price of 140 percent, the sale of bonds with par value of USD 3 billion would yield the GBRV Bs 9 billion.

End note.)

¶3. (SBU) Comment: We have noted in past reporting the apparent conviction of Merentes that a key to improving Venezuela's economy is controlling the parallel rate (ref B). We have also discussed two problems we see with this strategy, namely (1) the GBRV's economic model has far deeper problems than the gap between the parallel and official exchange rates; and (2) it will be very difficult for the GBRV to maintain effective control over the parallel rate in the medium term (ref C). (Note: Indeed Merentes, in an April 2008 meeting with Econoff well before he became BCV president, admitted that the issuance of dollar-denominated debt purchased in bolivars was not a sustainable method for controlling the parallel rate. End note.) Given the attractive implicit exchange rate and Venezuelans' incessant demand for dollars, we expect high demand for these bonds. It will be interesting to see whether the issuance drives the parallel rate down further and, if so, for how long. End comment.
DUDDY